Toward the mainstream: remittances and development in Latin America and the Caribbean
Manuel Orozco, Inter-American Dialogue; Testimony presented before the House Committee on Foreign Affairs, Subcommittee on the Western Hemisphere at the hearing entitled, "Leveraging Remittances for Families and Communities". October 2nd, 2007.

Dear members of Congress, Remittance transfers are one of the manifestations of contemporary transnational family ties and foreign labor mobility. Beyond the large volumes that are sustaining millions of families, these flows contribute to increase savings among recipient households, and in turn strengthen financial institutions and a country's economy. With appropriate policy tools the impact of these flows will have potential development implications in the countries where these flows are arriving and can help mitigate any new challenges. I will point out to four issues: the problems of remitting despite a demand for financial services, lessons learned when financial intermediation exists, current dynamics in the remittance environment and practical recommendations for U.S. cooperation.

I) Remittance transfers and lack of financial access: an urgent challenge
Migrants and their family are the main protagonists of international money transfers. Migrants are predominantly low income and financially disenfranchised with little access to the banking system. However, in order to fulfill their family obligations, they remit relatively fixed amounts of money [Exhibit 1] that reflect their home country's cost of living, which varies across Latin America and the Caribbean, and often represent 20 percent or more of their income earned in the United States.

Furthermore, the obligation to remit benefits everyone if migrants both have access to banking financial institutions (in the United States and their home country), and when they improve their legal status: Most migrants owning bank accounts send higher amounts, and invest in businesses back home. Moreover, most naturalized citizens who remit send more money back home. However, banking access is still very low among migrants in the U.S. [Exhibit 2]

Although the earnings received allow them to stay out of poverty and contribute significantly to build assets, as with migrants, receiving families are also financially out of the mainstream. Yet, the more transfers they collect, the higher the number of families with income that they can consider saving. They are more likely to take on bank accounts as well as other financial obligations. Financial access is incipient if not low. Although the percent of recipients with bank accounts is higher than among non recipients, the number of people with bank accounts is low, below 30%. Moreover, despite that banks pay most transfers of remittances there is poor financial intermediation among these institutions [Exhibit 3; [Exhibit 4].

II) When the supply meets the demand: leveraging remittances to promote financial access
There are exceptions however showing that when the supply of financial services caters to the demand of remittance recipients, financial access increases and the local economy benefits. For example, in rural areas in Mexico with high migration where banking institutions are not available, rural banks have stepped up to offer financial services, including remittance transfers. An association of rural banks, AMMUCS, for example, has increased its remittance services to this rural population, but people are also putting their money into savings: in the State of Puebla about 14% of remittances are saved in the Microbanco Pahuatlán. These savings contribute to a sustainable financial basis that the bank uses to finance productive activities. In turn, these activities generate income, jobs and some development.

Another case of providing financial services to recipients is the Mexican quasi-government agency BANSEFI which established a network, L@ Red de la Gente, of some 1200 banks, micro-finance institutions and credit unions. The goal is to serve as distribution centers for remittances. By September 2007, BANSEFI had increased its payments to 120,000 transfers and was opening accounts for about one quarter of its recipients [Exhibit 5].

An important example in financial intermediation is the experience of the Jamaica National Building Society (JNBS). Through its subsidiary, JN Money Services Ltd., JNBS serves Jamaicans living in the diaspora. By facilitating remittance services in Canada, the USA and the UK. In partnership and cooperation with USAID, JNBS chose to automate the process of sending and receiving money transfers through swipe card technology. It now has over 70,000 cards users. Moreover, fifty percent of remittance recipients in Jamaica have been brought into the formal banking system, with 40% of those receiving their remittances through a card product. The card product can also be used to make purchases at small businesses that accept debit cards. Savings rates have increased considerably through direct deposits to savings accounts. The amount of cash in circulation has gone down and the corollary use of electronic transactions is up.

In El Salvador some banks have also played a pivotal role. Banco Salvadoreño, the second largest commercial bank in El Salvador (with a migrant population in the United States in similar proportions to Moldova's migrants abroad), is an important example of the link between alliances with money transfer companies and banks and financial intermediation in El Salvador. Banco Salvadoreño has a presence in most U.S. states through its MTO, BancoSal, and strategic alliances with some of the biggest MTOs, including Western Union and Bancomer Transfer Services. In 2005, Banco Salvadoreño made over one million remittance payments, totaling $256 million. Ninety million were transfers from its own BancoSal, and 63 percent of BancoSal transfers were deposited directly into the accounts of at least 13,000 remittance recipients at Banco Salvadoreño. Banco Salvadoreño offers remittance recipients the opportunity to borrow up to 80 percent of their last six months' remittance flows. The bank has also opened more than 29,000 savings accounts for recipients and distributed nearly 9, 000 "Salvadoreño Emprendedor debit cards to small business owners and more than $10 million in loans to Salvadorans living abroad. In addition, Banco Salvadoreño is the only bank in El Salvador that has an Internet-based remittance service that enables clients to use the bank's website to send money from any account in the United States. The bank also offers a personalized service to its customers through a welcoming staff (Señoras de Bienvenida) who provide financial education on the spot to the families retrieving their remittance and encourage them to open bank accounts. Banco Salvadoreño is an example of a successful endeavor in banking remittance recipient families while offering a range of financial services.

III) The current environment: changing dynamics amidst the challenge of immigration reform

Amidst these trends, this year finds the remittance market faced with continued and additional challenges. The flow of remittances continues to increase and will likely reach 70 billion in 2007. Moreover, current trends in money transfers are shaping a process that signal different dynamics, some of which are interrelated. For example, growth of remittances to Mexico and some Central American countries has slowed, competition has increased through deepening and expanding of new businesses. Some of those trends are new while others are an intensification of previous developments. They are discussed here.

i) A Remittance slow down?

Year to year quarterly growth has slowed since mid 2006 and raised questions as to its causes [Exhibit 6, 7 & 8]. Many have argued that growth is associated to the crisis in the construction industry. However, there are other trends that bear attention, including the consequences of improved reporting.

The amounts reported today reflect an improvement in the accounting and reporting of money transfers by Money Transfer Operators (MTOs). Over the past five years, money transfer companies have increasingly reported their transactions to the Central Bank of Mexico, thus improving the recording of these flows and better reflecting actual migrant transfers.

In the late nineties and early 2000, competition grew as many companies began participating in the formal transfer process while at the same time financial institutions in Mexico entered into the business of paying transfers. One important example is the arrival of Bancomer Transfer Services, a company owned by BBVA-Bancomer, as a payment and processing platform. Since then, the company has been attracting and processing transfers from many MTOs and reporting its volumes to the Central Bank. Since 2000, their transactions have grown from fractions of percentages to over 40 percent of total volumes entering Mexico due to their introduction into the formal system.

For example, in early 2000 the Central Bank reported two million transfers. These figures were an underestimation and unrealistic because US Census data indicated that there were over ten million Mexican migrants in the country and survey data at the time showed that 70 percent of adult migrants were remitting, that is nearly six million people remitting.   A similar example reflects the methodological improvements by the Central Bank of Guatemala, which reflects improved reporting in 2001, date at which flows grew from 540 million to 1.5 billion.

Today Mexico's Central Bank statistics are reflecting seventy percent of the Mexican foreign labor force that sends money to their country, which amounts to nearly seven million people. Thus, the lower growth is associated in part to a statistical improvement in the amounts transferred. Furthermore, Central Bank data from other main recipient countries in the region indicate that the flows (including growth) continue to move in an upward trend.

Personal decisions and the immigration debate

The decline in quarterly growth also takes place during the U.S. immigration debate, increased immigration raids deporting undocumented migrants, predominantly, though not exclusively, Mexicans, and some state anti-immigration policies. Western Union, in fact, attributed the decline in their number of transactions to these concurrent events. Indeed, deportations have dramatically increased in the past three years -- doubling every year since 2004. Although in the short term the size of deportations, albeit the highest for the past ten years, do not have a strong effect in lowering the total amounts sent, they create fear and intimidation among migrants [Exhibit 9].

A recent survey commissioned by the Multilateral Investment Fund of the Inter-American Development Bank shows that nearly 40 percent of migrants said they were sending less or much less money as opposed to 20 percent who indicated sending more or a bit more. In balance, 18% of all respondents were sending less money, the majority (56%) of which was Mexicans migrants. Although it is uncertain by how much the decline amounts to, the difference between those sending less over those sending more (below US$350) was one tenth of one percent or about 6,000 people [Exhibit 10] [Exhibit 11].

Moreover, 55 percent of respondents agreed that the anti-immigration sentiment was making it more difficult for them to send more money back home. This is further notable considering the deportation statistics shown above, which give a sense of uncertainty and unease about the future [Exhibit 9].

A closer look at the data investigating what factors determined the sending of money indicates that earnings and the anti-immigration sentiment were strong statistically significant indicators of sending. A regression model was run using "sending more money" as a dependent variable with independent variables such as amount of hours worked, increased earnings, age, anti-immigration debate, and lack of jobs. The results show two statistically significant variables: the anti-immigration debate and increased earnings. The anti-immigration debate variable is statistically significant and negative, meaning that the greater the intensity of the debate the less money people were sending. Similarly, those earning more, were more likely to send more. This latter issue has proven to be a strong indicator of remitting, but the other variable ("anti-immigration debate") is a new factor [Exhibit 12].

Does the construction slowdown lead to a remittance slowdown?

Some news reports have argued that the decline in remittance growth is associated with an increase in unemployment among Latinos, particularly in the construction industry affected by the decline in real state prices. The argument is made on the consideration that one-fifth of Mexican workers are in the construction industry. Although there is no linear or statistically significant relationship suggesting that unemployment has led to a drop in remittances, the unemployment figures for last two quarters of 2006 and first two of 2007 do correlate negatively with the slow with growth [Exhibit 13].

Although most workers in construction are relatively mobile and seek to employ themselves in other sectors, over twenty percent of migrants who said were sending less, were also earning less money

(22%) or working less hours (29%). This may indicate that migrants may be sending less frequently while meeting their family obligation of taking care of the household.

ii. Competition in the money transfer business

Another continued trend is competition. A transformation in the US-LAC corridors is taking place whereby consolidation of firms has taking place. While pricing continues to decline, larger money transfer companies are losing market share to mid-size and emerging MTOs which started operating in the early 2000, and, on the demand side, migrants are turning to alternative methods of transfers.

In the first case at least eight companies have been acquired by outsider and insiders to the industry, including payment processing companies, banks or money transfer operators. These acquisitions have provided some clues as to the direction of where payments for migrant transfers may be heading in terms of market competition and product innovation.

For example, the list below shows the companies acquired, the acquirer and date of acquisition:

- Dolex (Global Payments) (2004);
- Ria (Euronet) (2007)
- Quisqueyana (Consorcio Mexicano) (2006)
- Vigo (Western Union) (2007)
- Uno (Omnex) (2005)
- Uniteller (BanNorte) (2007)
- GroupExpress (Coinstar) (2007)
- Multiservicios (Citibank) (2007)

Parallel to this trend two other dynamics refer to continued drops in pricing and the positioning of smaller companies and banking financial institutions. Many companies that have been operating for less than ten years have experienced important growth, while larger processors have lost market share. These smaller companies have grown since around 2005, increasing from less than 20,000 to nearly 200,000 monthly transactions. Consumer behavior has shifted from widely known Western Union, Sigue, MoneyGram or Dolex locations to newly recognized MTOs such as Viamericas, Reymesa or Alante Financial. These new companies' name branding is settling as part of the industry's consolidation as a legitimate money transfer provider.

More importantly, money transfer methods have slowly been shifting and diversifying beyond cash to cash transfers. A 2006 study of remittance senders in New York, New Jersey, Chicago, Miami, Washington, DC and Los Angeles showed that nearly three percent of transfers were handled by banks such as Wells Fargo, credit unions and Bank of America. This small share is related to their recent entrance into the market and the limited number of participating institutions. However, since 2000 at most one hundred financial banking and depository institutions have sought to attract remitters into the banking system by offering remittances transfer services and simultaneously provide typical financial services. Moreover, the survey showed that six percent of migrants have been using card based transfers. Nearly two percent of which are Mexican migrants using these alternative payment instruments.

A recent survey conducted in July 2007 showed that 7% of migrants were using U.S. banks to send money and another 5 percent were using debit cards or the internet. This trend signals a shift in the money transfer market that usually showed that more than 90% of consumers were using money transfer operators [Exhibit 14] .

Meanwhile pricing still matters both for suppliers and consumers. Transaction costs have continued a downward trend pushing some companies to look for value added services, expand to other corridors outside of Latin America or find other business opportunities [Exhibit 15] [Exhibit 16]. On the demand side consumers are manifesting a preference to shift from current cash to cash transfers and seek to adopt other methods, such as account to account transfers, card based transfers or mobile transfers.

Such preferences are also associated to the costs of the current transfer method, that is, those preferring to switch to a different method are paying more than those who don't want to change methods [Exhibit 17].

Related to these changes is remittance recording matters: not always these new methods are recorded in the Central Bank's balance of payments due to their methodology in recording transfers. This is particularly true of account to account transfers, whether they are performed via SWIFT, debit cards, online or with stored value cards. Therefore, some percent increase in transfers via account to account may not be recorded by the Central Bank, which only keeps data from wires via MTOs, checks, money orders, or the post office, and in turn may report a lower volume of transfers.

IV) The role of U.S. cooperation to leverage remittances

These experiences are suggesting an emerging trend among financial institutions to link up with recipients through the supply of financial services that in return can create growth. Opportunities for U.S. collaboration to facilitate strategies for financial intermediation can further accelerate development and leverage these flows promoting tools for self-sustainability that can improve wealth or protect families during times of adversity. Here we mention a few opportunities where institutions like USAID, the Millennium Challenge Corporation, the Inter-American Foundation, and the Overseas Private Investment Corporation could insert as development enablers through remittances.

i) Enabling technologies

New technologies can allow for cheaper account-to-account transactions. To do so, much is required. All market players must learn how to best use technologies. In terms of recipients, more financial education is needed alongside a change in understanding how money can be collected.

MTOs and banks should be encouraged to put technological devices for money transfers to practice. But technology solutions can be pricy. Incentives need to be clear, whether from the business case or coming from policy in the form of tax breaks for example. Consider point of sale (POS) devices. POS devices are an opportunity to enhance the effects of remittance by enabling electronic payments and lowering the hurdle when it comes to pulling revenue into the mainstream – into banks and MFIs. Cash that's in the bank is a form of savings and the trade-off to cash in pocket for pure consumption.

ii) Linking up

Financial institutions like micro-finance institutions (MFIs), credit unions and small banks have demonstrated a key role in banking the traditionally unbanked. This also means in transforming remittance clients into clients of financial services. Governments and donor countries have not been sufficiently supportive of MFIs, despite the latter's welcome efforts to reach out to remittance recipients.

Such links like that between a bank in an originating country and a microfinance institution at the destination have proven to be winning combinations. For example, a Spanish savings bank – Caxia Catalunya – established agreements with other banks and saving banks in Latin America. Some U.S. financial banking and non-banking institutions are starting to replicate these activities.

Another linking effort needs to target larger banks that offer remittance services. Access to additional banking services remains low despite the very high percentage of payments made by banks. The disconnect is made more stark when one considers that remittance transfer earnings represent 20% or more of their total net income. Throughout Latin America and the Caribbean, banks make nearly 50% of all remittance payments. Because of banks' roles in distributing remittances, it is particularly important that they move beyond simple remittance payments. They must offer financial literacy programs aimed at remittance recipients and opportunities to invest in assets and businesses.

iii) Financial literacy

A country's central bank often lacks the resources and capacity to provide basic financial literacy to their populations. Educating people about the role of finances is a critical step toward development. It is also becoming important among remittance recipients. Among the financially less literate, remitted money is more often spent on non-basic necessities. Training about the financial value of transfers as a mechanism to build credit and assets, for example, is indispensable.

iv) Making the most of remittances

If an economy is unable to produce in a competitive context, its labor force will be depressed and eventually a portion will migrate in order to take care of their families. The role of remittances in the lives of so many families is clearly dominant. But even once a member is away and sending money, the families may only be able to do so much with that money. It's up to the local economy to provide an effective supply of services and products.

The development challenge for business and policy practitioners worldwide is to catalyze the transformative role of remittances in a local economy. To pull the massive flows into the mainstream. Their work is to create appropriate conditions for a positive investment climate in their country of origin. Any effort to promote investment will not succeed if the business climate is not investor-friendly. All together, we are promoting development while at the same time, not telling migrants and their families what to do with their money. After all, while remittances are part of the transnational lifestyle, they are still in the family and family matters are private.

[EXHIBIT PRESENTATIONS]

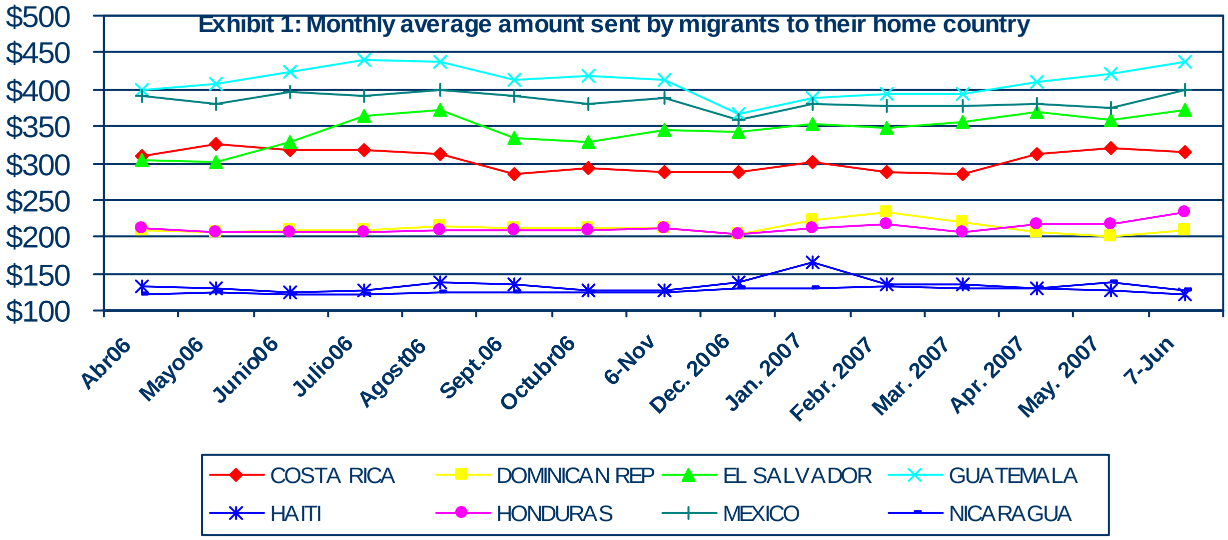
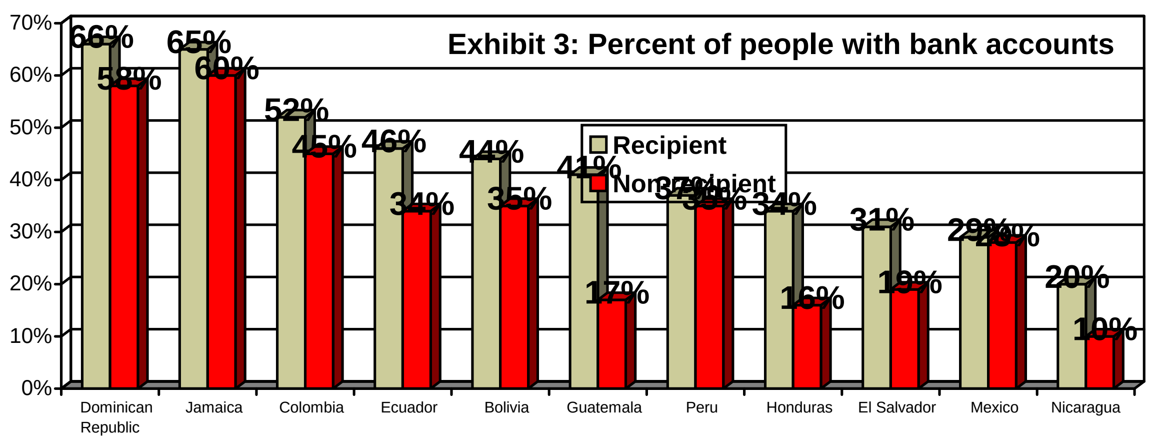


Exhibit 2: Remittances, banking and citizenship status

	Amount Sent ($)	(%) of all remitters
Owns checking account in home country	561	1
Has bank accounts in both countries	499	4
Has saving accounts in both countries	418	6
Owns a savings account in the home country	369	4
Remitter is naturalized U.S. citizen	342	19
Remits through banks	332	11
Owns checking account in the U.S.	267	30
Average remittance sent by all migrant remitters	265	
Owns savings account in the U.S.	254	31
Remits through money transfer companies	252	87

Source: Orozco, Manuel. Survey of Latinos remitting to Latin America, July 2007



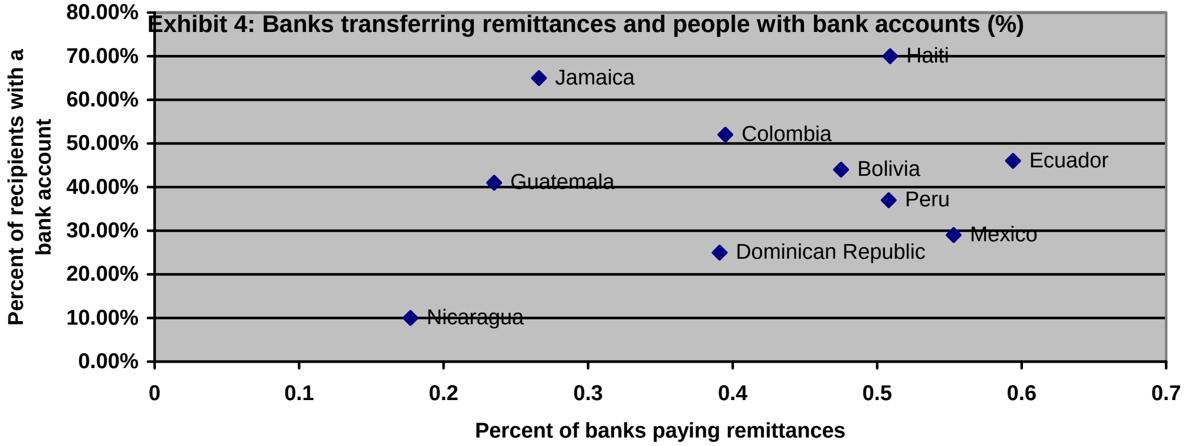


Exhibit 4: Banks transferring remittances and people with bank accounts (%)
Percent of recipients with a bank account
Percent of banks paying remittances
80.00%
70.00%
60.00%
50.00%
40.00%
30.00%
20.00%
10.00%
0.00%
0
0.1
0.2
0.3
0.4
0.5
0.6
0.7
Haiti
Jamaica
Colombia
Bolivia
Ecuador
Guatemala
Peru
Mexico
Dominican Republic
Nicaragua

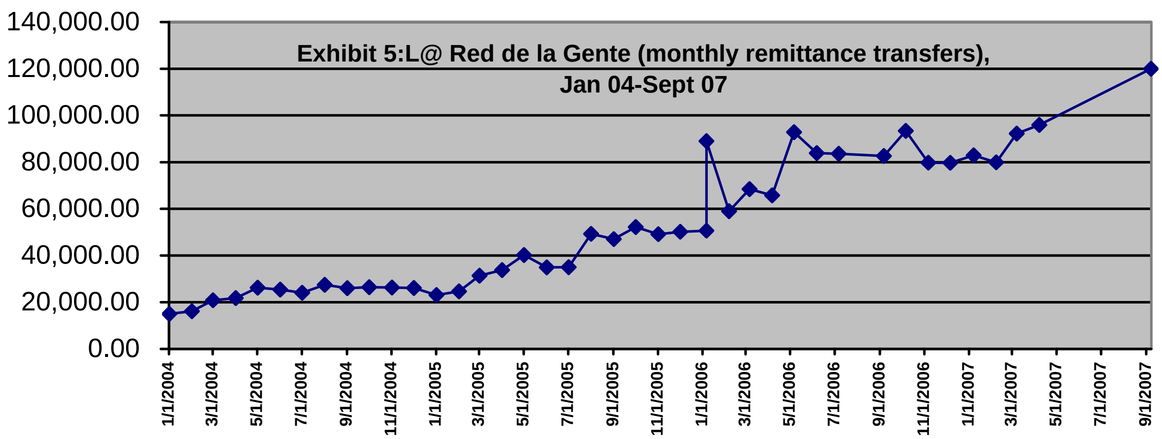


Exhibit 5:L@ Red de la Gente (monthly remittance transfers), Jan 04-Sept 07
140,000.00
120,000.00
100,000.00
80,000.00
60,000.00
40,000.00
20,000.00
0.00
1/1/2004
3/1/2004
5/1/2004
7/1/2004
9/1/2004
11/1/2004
1/1/2005
3/1/2005
5/1/2005
7/1/2005
9/1/2005
11/1/2005
1/1/2006
3/1/2006
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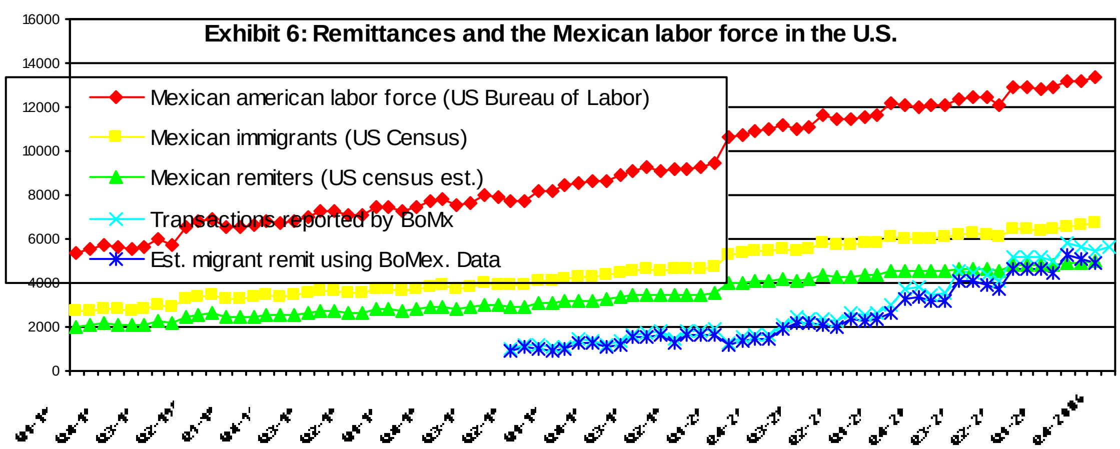
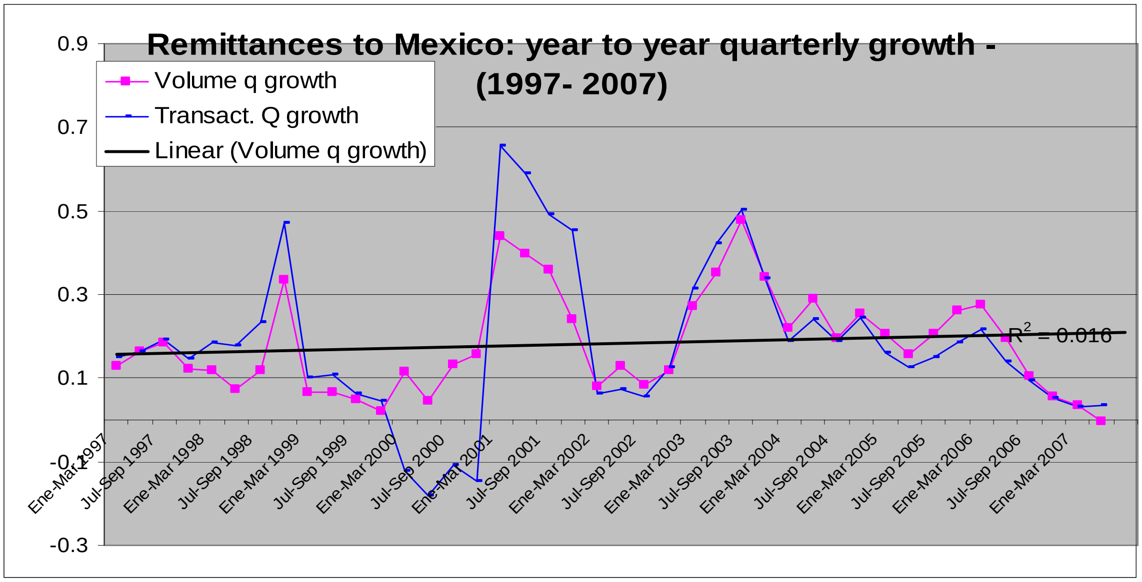


Exhibit 6: Remittances and the Mexican labor force in the U.S.
16000
14000
12000
10000
8000
6000
4000
2000
0
Mexican american labor force (US Bureau of Labor)
Mexican immigrants (US Census)
Mexican remiters (US census est.)
Transactions reported by BoMx
Est. migrant remit using BoMex. Data

Exhibit 7:



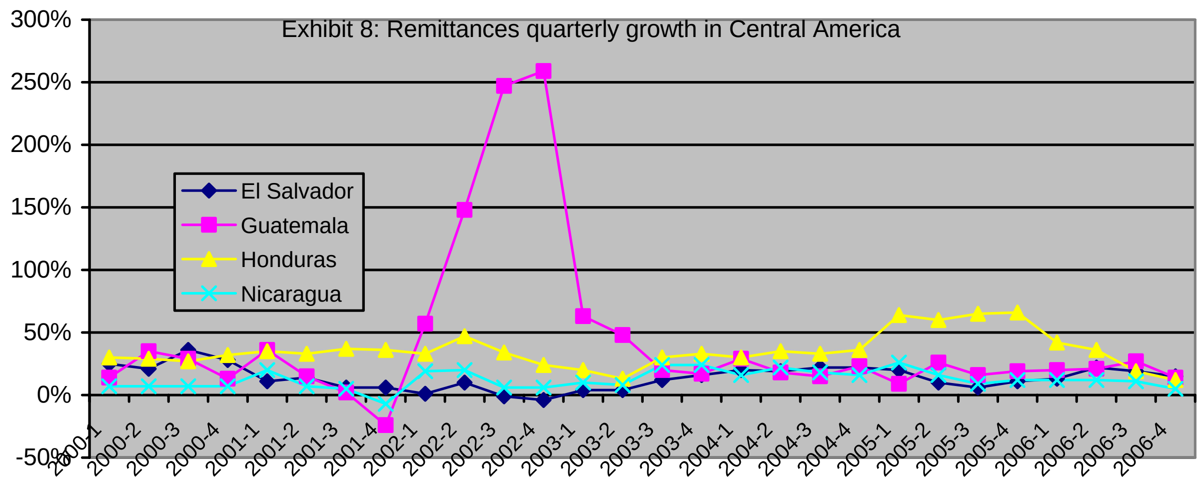


Exhibit 9: Deportations of Undocumented migrants in the U.S.

Countries	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007 [Jan-Jul]
Honduras	5,145	3,400	4,688	4,461	4,843	7,884	8,198	14,556	26,526	15,145
Dominican R	2,518	3,229	3,444	3,973	3,531	3,358	3,527	2,929	2,805	
El Salvador	5,348	4,048	4,617	3,808	3,902	5,108	6,405	7,235	10,312	10,954
Guatemala	5,152	3,429	4,222	4,343	4,919	6,848	8,308	12,529	18,386	11,458
Mexico	139,392	149,784	150,656	141,584	109,703	139,750	149,289	144,840	114,640	80,000
Nicaragua	411	406	459	500	445	656	793	1,022	2,241	1,800

Source: U.S. Immigration and Customs Enforcement

Exhibit 10: Migrants who say how much more or less they are remitting

	Percent
Much more money than last year	9
A little more money than last year	11
At about the same amount of money as last year	41
A little less money than last year	23
A lot less money than last year	15
Total	100.0

Exhibit 11: Migrants responding whether they are sending more or less remittances this year

	Mexico	Guatemala	Honduras	El Salvador	All four countries
Less or much less money sent	22%	7%	3%	8%	39%
Much more, more or the same money sent	32%	11%	3%	15%	62%

Exhibit 12: Regression Results for sending more money

	B	S.E.	Wald	df	Sig.	Exp(B)
Length of time in the U.S.	-.174	.149	1.354	1	.245	.840
Employment position	.087	.203	.186	1	.667	1.091
Length of time at current job	-.040	.145	.074	1	.785	.961
Legal status	.196	.288	.466	1	.495	1.217
Gender	.088	.274	.104	1	.747	1.092
Lack of jobs	.357	.349	1.049	1	.306	1.430
Earning more than last year	***.730***	***.166***	***19.363***	***1***	***.000***	***2.075***
Anti-immigration debate makes it difficult to remit	***-.355***	***.256***	***1.918***	***1***	***.166***	***.701***
Age	.030	.146	.043	1	.836	1.031
Constant	-3.077	1.571	3.837	1	.050	.046

Exhibit 14: Use of remittance card

Remittance card	Mexico	D.R.	Jamaica	El Salv.	Guatem	Boliv.	Nicarag.	Total
Percent	*1.8*	*5.0*	*6.5*	*12.8*	*1.0*	*8.0*	*13.0*	*6.3*

Source: Orozco, Manuel. Card based transfers study, 2007.

Exhibit 15:Percent of people using banks for Money transfers: 1.00% (2004); 3% (2006); 7% (2007)